



Vermont (State of)

Contacts

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Moody's Rating

| Issue | Rating |
|--|--------------------|
| General Obligation Refunding Bonds 2004 Series A | Aa1 |
| Sale Amount | \$118,595,000 |
| Expected Sale Date | 02/04/04 |
| Rating Description | General Obligation |

MOODY'S ASSIGNS Aa1 RATING TO STATE OF VERMONT'S GENERAL OBLIGATION BONDS

OUTLOOK REMAINS STABLE

Opinion

Moody's has assigned a rating of Aa1 and stable outlook to the State of Vermont's general obligation bonds. The state's high quality rating reflects Vermont's stable financial position with increased reserve levels; relatively strong economic performance during the recent recession with some delay in the state's recovery reflecting continued weakness in Vermont's manufacturing sector; and manageable debt levels that have declined over the past few years. At the end of fiscal 2003, Vermont added to its General Fund Budget Stabilization Reserve (BSR) to begin replenishing funds used to offset revenue weakness in the prior year (fiscal 2002). Vermont's most recent revenue forecast (January 2004) for fiscal 2004 shows that revenues are ahead of target for the first six months. The fiscal 2004 budget calls for full restoration of the state's BSR's in the General, Transportation, and Education Funds.

Vermont plans to sell approximately \$118 million in General Obligation Refunding Bonds, 2004 Series A on February 4th for debt service savings.

STRUCTURAL BUDGET BALANCE REFLECTS SOUND FINANCIAL MANAGEMENT

Conservative budgeting and favorable tax revenue performance allowed Vermont to produce operating surpluses that brought the General Fund BSR to approximately \$43 million at 2001 year-end. However Vermont was not immune to the recent recession. As the economy and State revenues weakened in fiscal 2002 General Fund revenue projections were twice revised downward from original estimates and appropriation levels were also reduced. Between fiscal years 2001 and 2002, personal income taxes

(Vermont's largest revenue source in the General Fund) dropped 10%, while sales and use taxes were essentially flat. At year-end fiscal 2002, the state recorded a General Fund operating deficit of \$29.5 million after required transfers to the Transportation Fund (\$13.85 million) and Education Fund (\$5.6 million). The State eliminated the deficit by dipping into the General Fund Budget Stabilization Reserve Fund, still leaving a balance of nearly \$18 million in the reserve.

Revenue collections improved in fiscal 2003 and total tax revenues grew nearly 5% over the prior year, after dropping 6% between fiscal years 2001 and 2002. Vermont received \$50 million in federal relief funds which were applied for one-time uses rather than base-building. A slight General Fund operating deficit was offset by transfers from the transportation fund and the tobacco settlement fund. At year end fiscal 2003, the state increased its General Fund BSR, bringing it to \$23.6 million, and also recorded a balance of \$11.2 million the Education Fund BSR, both half of the statutory maximum of 5% of prior year budgetary appropriations. The Human Services Caseload Reserve Fund, which is available for unexpected caseload growth due to the economy, was down slightly to \$17.2 million at the end of fiscal 2003. The fiscal 2004 budget includes an increase in the Caseload Reserve Fund to \$24.7 million.

FISCAL YEAR 2004 REVENUE PERFORMANCE AHEAD OF TARGET

Vermont's most recent consensus revenue forecast (January 2004) indicates that General Fund revenues are running about 5% ahead of target, with all major tax sources performing well. Adjusting for the 1 cent sales tax increase (from 5% to 6%) effective October 2003, revenues are still up over the prior year. The state expects Budget Stabilization Reserves in the General, Transportation, and Education Funds to be fully funded at the end of fiscal 2004.

Growth in Education Fund revenues is also higher than expected, largely due to increasing property values leading in turn to higher property tax receipts. As a result, the governor has proposed a 5 cent (per \$100 valuation) reduction in the state's property tax rate.

MODEST ECONOMIC IMPROVEMENT; MANUFACTURING SECTOR REMAINS WEAK

Vermont's economy held up relatively well in the recent recession. Unemployment levels hovered around 4.0% for most of calendar year 2003, slightly higher than in 2002 but still about 2 percentage points below national unemployment rates, and lower than other New England States. As in other states, particularly those with a significant manufacturing sector presence, Vermont's economic recovery has been sluggish so far.

Manufacturing remains one of the core industries of Vermont's economy although the sector has declined as a percentage of industry employment as jobs have been shed. Manufacturing made up 13.6% of Vermont's non-farm employment versus 11.7% for the United States in 2002. In prior years manufacturing accounted for nearly 16% of the state's non-farm employment, versus national averages of about 13%. Tourism remains a vital source of seasonal cash flow from income and sales tax revenue for Vermont. Tourism-sensitive revenues performed reasonably during the recession and show signs of growth in the near term forecast.

Vermont's economic performance is not expected to begin expanding until the fourth quarter of calendar year 2004, delayed one quarter from the state's previous economic forecast in May 2003. While the state has seen some labor market improvement, with the recovery of about one-third of total jobs lost during the recession, the state's manufacturing sector remains weak. IBM, the state's largest employer, reduced about 1,800 jobs over the past two years, including 514 permanent job reductions in October

2003. Given the recent sharp increase in international competition for still relatively weak global demand in high tech industries, IBM's employment levels could deteriorate further.

ABOVE AVERAGE LEVELS OF RAPIDLY AMORTIZED DEBT; MODEST ISSUANCE PLANNED

Vermont's debt levels are moderately high relative to other states, on both a per capita and personal income basis although the state's ratios have declined slightly in recent years. Debt per capita of \$861, compared to the state median of \$606, ranked Vermont sixteenth among the fifty states in 2003. Debt to total personal income of 2.9%, compared to the 2.2% state median, ranked seventeenth representing an improvement over prior years. The state's debt authorization levels have dropped steadily over the past decade. The amount for 2004 is about two-thirds of the level authorized in 1995.

Vermont plans to issue a total of approximately \$42.2 million in bonds for capital projects in 2004, including \$3.2 million authorized but unissued in fiscal 2003. The state issued short term notes to meet cash flow needs in the past two years - \$75 million in fiscal year 2003 and \$48 million in fiscal year 2004. The fiscal 2004 notes are due on March 5, 2003 and the state has no further short-term borrowing plans for the current fiscal year.

Outlook

Vermont's credit outlook is stable, reflecting growth in the state's primary revenue sources, increasing reserve levels, and the state's demonstrated ability to respond with budget adjustments as needed to maintain budget balance. Favorable operating performance in the years prior to the most recent recession allowed the state to build and maintain reserve funds at 5% of the prior year budgetary appropriations in each of the General, Transportation and Education Funds. These funds provided a degree of operating cushion, making the state well positioned to accommodate revenue shortfalls that occurred in fiscal 2002. Vermont's commitment to restoration of reserve levels, with full funding expected at the end of fiscal 2004, reflects the state's sound financial management and conservative fiscal policies.